

OTTUMWA WATER WORKS
OTTUMWA, IOWA

INDEPENDENT AUDITOR'S REPORT
BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
SCHEDULE OF FINDINGS

DECEMBER 31, 2008

OTTUMWA WATER WORKS

TABLE OF CONTENTS
DECEMBER 31, 2008

	<u>PAGE</u>
<u>OFFICIALS</u>	1
<u>INDEPENDENT AUDITOR'S REPORT</u>	2
<u>MANAGEMENT'S DISCUSSION AND ANALYSIS</u>	3-5
	<u>EXHIBIT</u>
<u>BASIC FINANCIAL STATEMENTS:</u>	
STATEMENT OF NET ASSETS	A 6
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS	B 7
STATEMENT OF CASH FLOWS	C 8
NOTES TO FINANCIAL STATEMENTS	9-15
<u>REQUIRED SUPPLEMENTARY INFORMATION:</u>	
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS AND CHANGES IN BALANCES – BUDGET AND ACTUAL	16
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION – BUDGETARY REPORTING	16
<u>OTHER SUPPLEMENTARY INFORMATION:</u>	
DETAIL SCHEDULE OF REVENUES AND EXPENSES	17-18
INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS	19-20
SCHEDULE OF FINDINGS	21-22

OTTUMWA WATER WORKS

OFFICIALS
DECEMBER 31, 2008

<u>NAME</u>	<u>TITLE</u>	<u>TERM EXPIRES</u>
Teri Messerschmitt	Water Works Trustee	July, 2013
Pete Rich	Water Works Trustee	July, 2014
Clive Parcell	Water Works Trustee	July, 2009
Bruce Turner	Water Works Trustee	July, 2010
Jack Kirk	Water Works Trustee	July, 2012
Rodney Hamilton	Interim General Manager	Indefinite

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Ottumwa Water Works
Ottumwa, Iowa

We have audited the accompanying financial statements of Ottumwa Water Works as of and for the year ended December 31, 2008. These financial statements are the responsibility of Ottumwa Water Works' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Ottumwa Water Works as of December 31, 2008, and the changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated August 7, 2009 on our consideration of the Utility's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and important for assessing the results of our audit.

The management's discussion and analysis and budgetary comparison information on pages three through five and sixteen are not a required part of the basic financial statements, but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Utility's basic financial statements. We previously audited, in accordance with the standards referred to in the second paragraph of this report, the financial statements for the three years ended December 31, 2007 (which are not represented herein) and expressed unqualified opinions on those financial statements. Other supplementary information is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

ANDERSON, LARKIN & CO. P.C.

Ottumwa, Iowa
August 7, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS

Ottumwa Water Works provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the calendar year ended December 31, 2008. We encourage readers to consider this information in conjunction with the Utility's financial statements which follow.

FINANCIAL HIGHLIGHTS

The Utility's operating revenues decreased by approximately 5.7% or \$282,301 from 2007 to 2008. Decreases in revenue from the sale of water accounted for the majority of the decrease.

The Utility's operating expenses increased approximately 12.2% or \$495,040 from 2007 to 2008. This increase included a \$228,859 increase in general plant expenses.

The Utility's net assets increased approximately 1.5% or \$332,965 from 2007 to 2008.

USING THIS ANNUAL REPORT

The Ottumwa Water Works is a publicly owned utility and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting which is the same measurement focus and basis of accounting employed by private sector business enterprises. This discussion and analysis is intended to serve as an introduction to Ottumwa Water Work's basic financial statements. The annual report consists of a series of financial statements and other information as follows:

Management's Discussion and Analysis introduces the basic financial statements and provides an analytical overview of the Utility's financial activities.

The Statement of Net Assets presents information about the Utility's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Utility is improving or deteriorating.

The Statement of Revenues, Expenses and Changes in Net Assets is the basic statement of activities for proprietary funds. This statement presents information on the Utility's operating revenues and expenses, non-operating revenues and expenses and whether the Utility's financial position has improved or deteriorated as a result of the year's activities.

The Statement of Cash Flows presents the change in the Utility's cash and cash equivalents during the year. This information can assist the user of the report in determining how the Utility financed its activities and how it met its cash requirements.

The Notes to Financial Statements provide additional information essential to a full understanding of the data provided in the basic financial statements.

FINANCIAL ANALYSIS OF THE UTILITY

Statement of Net Assets

As noted earlier, net assets may serve over time as a useful indicator of the Utility's financial position. The Utility's net assets as of December 31, 2008 total \$22,541,173. This compares to \$22,208,208 as of December 31, 2007. A summary of the Utility's net assets as of December 31, 2008 and 2007 are presented below.

NET ASSETS

	<u>December 31,</u>	
	<u>2008</u>	<u>2007</u>
Current assets	\$ 6,753,940	\$ 7,045,065
Capital assets at cost, less accumulated depreciation	25,963,439	24,815,139
Other assets	<u>98,112</u>	<u>81,484</u>
Total assets	<u>32,815,491</u>	<u>31,941,688</u>
Current liabilities	1,964,182	2,090,351
Long-term liabilities	<u>8,310,136</u>	<u>7,643,129</u>
Total liabilities	<u>10,274,318</u>	<u>9,733,480</u>
Unrestricted assets	5,264,228	5,178,394
Invested in capital assets, net of related debt	17,276,945	16,848,010
Restricted assets	<u>-</u>	<u>181,804</u>
Total net assets	<u>\$ 22,541,173</u>	<u>\$ 22,208,208</u>

Statements of Revenues, Expenses and Changes in Net Assets

Operating revenues are received from the sale of water to Ottumwa residents, sale of hydro electric power, and other miscellaneous income. Non-operating revenues and expenses include interest income. The utilization of capital assets is reflected in the financial statements as depreciation, which allocates the cost of an asset over its expected useful life. A summary of revenues, expenses and changes in net assets for the years ended December 31, 2008 and 2007 is presented below:

CHANGES IN NET ASSETS

	<u>Year Ended December 31,</u>	
	<u>2008</u>	<u>2007</u>
Operating revenue:		
Sale of water	\$ 3,518,691	\$ 3,735,085
Sale of electricity	831,327	885,684
Miscellaneous income	<u>306,206</u>	<u>317,756</u>
Total operating revenue	<u>4,656,224</u>	<u>4,938,525</u>
Operating expenses:		
Production	673,449	649,500
Distribution	687,920	700,372
Hydro	132,970	134,326
Financial services	275,785	241,973
Administration	467,510	453,437
General plant	1,283,167	1,054,308
Depreciation and amortization	<u>1,026,412</u>	<u>818,257</u>
Total operating expenses	<u>4,547,213</u>	<u>4,052,173</u>
Operating income	109,011	886,352
Nonoperating revenue:		
Interest income	<u>223,954</u>	<u>263,894</u>
Change in net assets	332,965	1,150,246
Net assets – Beginning of year, as restated	<u>22,208,208</u>	<u>21,057,962</u>
Net assets – End of year	<u>\$ 22,541,173</u>	<u>\$ 22,208,208</u>

The Statement of Revenues, Expenses and Changes in Net Assets reflects a positive year with an increase in the net assets at the end of the year.

During calendar year 2008, operating revenues decreased 5.7%, or \$282,301, due in part to decreased sales of water. Operating expenses increased approximately 12.2% or \$495,040. This increase included a \$228,859 increase in general plant expenses.

Statement of Cash Flows

The Statement of Cash Flows presents information related to cash inflows and outflows, summarized by operating, capital and related financing activities and investing activities. Cash flows from operating activities include the sale of water, electricity and other receipts reduced by payments to suppliers and employees. Cash flows from capital and related financing activities include the purchase of capital assets. Cash flows from investing activities include interest income and the purchase and redemption of certificates of deposit. Cash flows from financing activities include proceeds and payments related to the Utility's debt.

Budget

The Utility submits a budget to the City of Ottumwa on an annual basis. Receipts for the year exceeded the amounts budgeted by \$274,089 and disbursements exceeded amounts budgeted by \$102,183.

CAPITAL ASSETS

At December 31, 2008, the Utility had \$25,963,439, invested in capital assets, net of accumulated depreciation of \$20,442,400. Depreciation and amortization charges totaled \$1,026,412 for the year. More detailed information about the Utility's capital assets is presented in the Notes to Financial Statements.

LONG-TERM DEBT

At December 31, 2008, the Utility had \$8,686,494 in total long-term debt outstanding. During the year ended December 31, 2008, the Utility issued a total of \$1,077,050 of long-term debt to finance Utility construction projects. Additional information regarding the Utility's long-term debt is included in the Notes to Financial Statements.

ECONOMIC FACTORS

Ottumwa Waters Works continued to improve its financial position during the current calendar year. However, the current condition of the economy in the State continues to be a concern for Utility officials. Some of the realities that may potentially become challenges for the Utility to meet are:

The Utilities distribution system requires constant maintenance and upkeep.

The continued inflationary increases in health care, chemical, and energy costs.

Technology continues to expand and current technology becomes outdated presenting an on-going challenge to maintain up to date technology at a reasonable cost.

The Utility anticipates the current year will be much like the last and we will maintain a close watch over resources to maintain our ability to react to unknown issues.

CONTACTING THE UTILITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, customers and creditors with a general overview of the Utility's finances and to show the Utility's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Ottumwa Water Works, P.O. Box 20, Ottumwa, Iowa.

OTTUMWA WATER WORKSSTATEMENT OF NET ASSETSDECEMBER 31, 2008ASSETSCURRENT ASSETS:

Cash and cash equivalents	\$ 847,268
Certificates of deposit	4,530,000
Accounts receivable, net of allowance for uncollectible accounts	1,187,073
Inventory	159,453
Accrued interest receivable	11,238
Prepaid expenses	18,908
Total current assets	<u>6,753,940</u>

CAPITAL ASSETS:

Buildings	6,069,132
Water distribution system	37,287,371
Equipment and vehicles	1,593,665
Office equipment	647,875
Total	<u>45,598,043</u>
Less accumulated depreciation	<u>20,442,400</u>
Depreciated value of capital assets	25,155,643
Land	618,577
Construction in progress	189,219
Total capital assets	<u>25,963,439</u>

OTHER ASSETS:

Deferred charges - Debt issue costs	<u>98,112</u>
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TOTAL ASSETS	<u>32,815,491</u>
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CURRENT LIABILITIES:

Accounts payable	127,972
Accrued payroll and related expenses	38,311
Accrued interest	31,998
Sales tax	5,963
Sick leave	172,448
Accrued vacation	63,747
Self insurance	25,637
Accrued disability and life insurance	124,825
Customer deposits	187,462
Current maturities of long-term debt	376,358
Accrued sewer and refuse collections	809,461
Total current liabilities	<u>1,964,182</u>

LONG-TERM DEBT - Less current maturities8,310,136

TOTAL LIABILITIES	<u>10,274,318</u>
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NET ASSETS:

Unrestricted	5,264,228
Invested in capital assets, net of related debt	<u>17,276,945</u>
TOTAL NET ASSETS	\$ <u>22,541,173</u>

See Accompanying Notes to the Financial Statements

OTTUMWA WATER WORKSSTATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEAR ENDED DECEMBER 31, 2008OPERATING REVENUE:

Sale of water	\$ 3,518,691
Sale of electricity	831,327
Miscellaneous income	<u>306,206</u>
Total operating revenue	<u>4,656,224</u>

OPERATING EXPENSES:

Production	673,449
Distribution	687,920
Hydro	132,970
Financial services	275,785
Administration	467,510
General plant	1,283,167
Depreciation and amortization	<u>1,026,412</u>
Total operating expenses	<u>4,547,213</u>

OPERATING INCOME	109,011
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NONOPERATING REVENUE:

Interest income	<u>223,954</u>
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CHANGE IN NET ASSETS	332,965
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<u>NET ASSETS</u> - BEGINNING OF YEAR, AS RESTATED	<u>22,208,208</u>
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<u>NET ASSETS</u> - END OF YEAR	\$ <u>22,541,173</u>
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OTTUMWA WATER WORKSSTATEMENT OF CASH FLOWS
YEAR ENDED DECEMBER 31, 2008CASH FLOWS FROM OPERATING ACTIVITIES :

Cash received from customers	\$ 4,234,538
Cash received from other operating receipts	306,206
Cash paid to suppliers for goods and services	(2,517,799)
Cash paid to employees for services	(1,201,474)
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>821,471</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES :

Purchase of capital assets	(1,599,534)
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CASH FLOWS FROM INVESTING ACTIVITIES :

Interest on investments	218,869
Purchase of certificates of deposit	(4,530,000)
Proceeds from certificates of deposit	<u>1,930,000</u>
NET CASH USED IN INVESTING ACTIVITIES	<u>(2,381,131)</u>

CASH FLOWS FROM FINANCING ACTIVITIES :

Proceeds from long-term debt	485,243
Principal payments on long-term debt	(357,685)
NET CASH PROVIDED BY FINANCING ACTIVITIES	<u>127,558</u>

NET DECREASE IN CASH AND CASH EQUIVALENTS (3,031,636)

CASH AND CASH EQUIVALENTS - Beginning of year

3,878,904

CASH AND CASH EQUIVALENTS - End of year

\$ 847,268

RECONCILIATION OF OPERATING INCOME TO NET CASH
PROVIDED BY OPERATING ACTIVITIES :

Operating income	\$ 109,011
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation and amortization expense	1,026,412
Change in operating assets and liabilities:	
Increase in accounts receivable	(115,480)
Increase in inventory	(21,635)
Decrease in prepaid expenses	1,690
Decrease in accounts payable	(413,135)
Increase in accrued payroll and related expenses	13,788
Increase in accrued interest	11,463
Increase in sales tax	5,963
Decrease in sick leave	(8,102)
Increase in accrued vacation	1,847
Increase in self insurance	9,247
Increase in accrued disability and life insurance	23,465
Increase in customer deposits	16,972
Increase in accrued sewer and refuse collections	<u>159,965</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ <u>821,471</u>

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION :

Cash paid for interest (\$242,863 capitalized)	\$ <u>260,351</u>
Debt issue costs paid by issuance of additional long-term debt	\$ <u>21,628</u>
Fixed assets acquired by issuance of long-term debt	\$ <u>570,180</u>

See Accompanying Notes to the Financial Statements

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Ottumwa Water Works is organized as a municipal water utility which was established in 1910. They are overseen by a five member board appointed by the City Council and Mayor of the City of Ottumwa. The Utility's operating budget is subject to the approval of the City Council. The Water Works is considered by the City of Ottumwa to be substantially autonomous. The Water Works is funded entirely by water user charges collected from users of the Water Works' system.

The financial statements of the Water Works are prepared in conformity with U.S. generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board.

Reporting Entity

For financial reporting purposes, Ottumwa Water Works has included all funds, organizations, agencies, boards, commissions and authorities. The Utility has also considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to or impose specific financial burdens on the Utility. Ottumwa Water Works has no component units which meet the Governmental Accounting Standards Board criteria.

Ottumwa Water Works is not presented as a Component Unit in the City of Ottumwa's financial statements. The Utility is a legally separate entity from the City, but is financially accountable to the City. The Utility is governed by a five-member Board appointed by the City Council and the Utility's operating budget is subject to the approval of the City Council.

Basis of Presentation

The accounts of the Ottumwa Water Works are organized as an enterprise fund. Enterprise funds are used to account for operations (a) financed and operated in a manner similar to private business enterprises, where the intent of the governing body is the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or (b) where the governing body has decided periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability or other purposes.

Measurement Focus and Basis of Accounting

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The Ottumwa Water Works applies all applicable GASB pronouncements, as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements; Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Ottumwa Water Works distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Assets

The following accounting policies are followed in preparing the Statement of Net Assets:

Cash, Investments and Cash Equivalents – The Ottumwa Water Works considers all short-term investments that are highly liquid to be cash equivalents. Cash equivalents are readily convertible to known amounts of cash and, at the day of purchase, have a maturity date no longer than three months. Cash investments not meeting the definition of cash equivalents at December 31, 2008 include certificates of deposit of \$4,530,000.

Accounts Receivable – Ottumwa Water Works grants credit to customers, substantially all of whom are located in Ottumwa, Iowa. The risk of loss on the accounts receivable is the balance due at the time of default. Accounts receivable are considered past due after 30 days and are charged off when management determines the account is uncollectible. The Ottumwa Water Works uses the reserve method of accounting for uncollectible accounts. At December 31, 2008, a reserve of \$99,343 is provided to allow for uncollectible customer accounts.

Material and Chemicals Inventory – Inventories are stated at the lower of cost (determined on a first-in, first-out basis) or market.

During 1992, the Ottumwa Water Works changed its purchased material goods inventory to carry only selected groups of items and material individual items over a predetermined dollar amount. All other small parts and immaterial cost items will be expensed when purchased.

Capital Assets – Capital assets are accounted for at historical cost. Depreciation of all exhaustible capital assets is charged as an expense against operations. The cost of repair and maintenance is charged to expense, while the cost of renewals or substantial betterments is capitalized. The cost and accumulated depreciation of assets disposed of are deleted, with any gain or loss recorded in current operations.

Reportable capital assets are defined by the Utility as assets with initial, individual costs in excess of the following thresholds and estimated useful lives in excess of one year

<u>Asset Class</u>	<u>Amount</u>
Buildings	\$ 500
Water distribution system	500
Equipment and vehicles	500
Office equipment	500

Capital assets of the Utility are depreciated using the straight line method over the following estimated useful lives:

<u>Asset Class</u>	<u>Estimated Useful lives (In years)</u>
Buildings	15-25
Water distribution system	40-50
Equipment and vehicles	5-7
Office equipment	5-7

Interest is capitalized on qualified assets acquired with certain tax-exempt debt. The amount of interest to be capitalized is calculated by offsetting interest expense incurred from the date of the borrowing until completion of the project with interest earned on invested proceeds over the same period. Current year capitalized interest relates to current construction in progress projects.

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Compensated Absences – Utility employees accumulate a limited amount of earned but unused vacation hours for subsequent use or for payment upon termination, death or retirement. The Utility's liability for accrued vacation has been computed based on rates of pay in effect at December 31, 2008.

Use of Estimates - Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Accordingly, actual results could differ from those estimates.

Budgets and Budgetary Accounting – The Budgetary comparison and related disclosures are reported as Required Supplementary Information. During the year ended December 31, 2008, disbursements exceeded the amounts budgeted.

NOTE 2 – CASH AND INVESTMENTS

The Utility's deposits in banks at December 31, 2008 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against depositories to insure there will be no loss of public funds.

The Municipal Utility is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Utility Board of Trustees; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

NOTE 3 – CAPITAL ASSETS

A summary of capital assets at December 31, 2008 is as follows:

	Balance December 31, 2007 <u>As Restated</u>	Additions/ Reclassifications	Deletions/ Reclassifications	Balance December 31, 2008
Capital assets, being depreciated:				
Buildings	\$ 3,225,576	\$ 2,843,556	\$ -	\$ 6,069,132
Water distribution system	35,631,967	1,655,404	-	37,287,371
Equipment and vehicles	1,522,950	70,715	-	1,593,665
Office equipment	623,493	24,382	-	647,875
Total capital assets, being depreciated	41,003,986	4,594,057	-	45,598,043
Less accumulated depreciation	19,420,988	1,021,412	-	20,442,400
Total capital assets being depreciated, net	21,582,998	3,572,645	-	25,155,643
Capital assets, not being depreciated:				
Land	618,577	-	-	618,577
Construction in progress	2,613,564	1,638,750	4,063,095	189,219
Capital assets, net	\$ 24,815,139	\$ 5,211,395	\$ 4,063,095	\$ 25,963,439

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS

NOTE 4 – PENSION AND RETIREMENT BENEFITS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P O. Box 9117, Des Moines, Iowa, 50306-9117.

Plan members are required to contribute 3.90% and 4.10% of their annual covered salary and the Utility is required to contribute 6.05% and 6.15% of annual covered payroll for the years ended June 30, 2007 and 2008, respectively. Contribution requirements are established by state statute. The Utility's contributions to IPERS for the years ended December 31, 2008, 2007 and 2006 were \$73,387, \$71,432, and \$67,794 respectively, equal to the required contributions for each year.

NOTE 5 – SELF INSURANCE PROGRAM

The Utility has a self-insurance program for hospitalization and medical coverage for its employees. The program is administered through a service agreement with Cottingham Butler. The Utility limits its losses through the use of stop-loss policies from reinsurers. Specific individual losses for claims are limited to \$20,000 a year. The Utility's aggregate annual loss limitation is based on a formula that considers, among other things, the total number of employees. For December 31, 2008, the Utility incurred \$353,747 in expense under the program.

Amounts payable by Ottumwa Water Works at December 31, 2008 total \$25,637 which is for incurred but not reported (IBNR) and reported but not paid claims. The amounts are based on estimates of the amounts necessary to pay prior-year and current-year claims. A liability has been established based on the requirements of Governmental Accounting Standards Board Statement Number 10, which requires that a liability for claims be reported if information prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. Settlements have not exceeded the stop-loss coverage in any of the past three years. A reconciliation of changes in the aggregate liability for claims for the current year is as follows:

Unpaid claims as of December 31, 2007	\$ 16,390
Incurred claims (including claims incurred but not reported as of December 31, 2008):	
Provision for current-year events where the Utility has retained risk of loss	353,747
Payments:	
Claims attributable to current-year events where the Utility has retained risk of loss	<u>344,500</u>
Unpaid claims as of December 31, 2008	\$ <u>25,637</u>

NOTE 6 – OTHER EMPLOYEE BENEFITS

The Water Works employees accumulate sick leave and vacation hours for subsequent use. The liability for accrued vacation at December 31, 2008 is \$63,747. The Water Works has a policy of paying one-half of the unused accumulated sick leave upon retirement of any employee. The maximum number of days an employee can accumulate is 120. Upon the death of any employee, 100% of the accumulated sick leave is paid. One-half of unused sick leave totals \$172,448, and is reflected in the financial statements as a liability at December 31, 2008.

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS

NOTE 6 – OTHER EMPLOYEE BENEFITS (Continued)

Effective November 1, 1989, the Water Works began a long-term disability plan. Once an employee has accumulated the maximum number of days of sick leave referred to in the preceding paragraph, they begin to accumulate long-term disability days. The days are accumulated at 50% of the normal sick leave accrual rate, and the maximum number of days to be accrued is 120. The compensation is computed at 60% of the employee's normal salary and is paid only after all normal sick leave benefits are exhausted.

The amount of the accrual reflected on the balance sheet at December 31, 2008 for the long-term disability benefit is \$116,825.

NOTE 7 – POST RETIREMENT BENEFITS

On July 22, 1992, the Ottumwa Water Works approved a policy to drop the group term life insurance coverage on existing retirees and instead pay a one-time death benefit equal to the term coverage in effect as of this date. The total death benefit payable as of December 31, 2008 was \$8,000 and covers eight retirees. Only these eight retirees are covered by this provision. Any other employees retiring on or after July 22, 1992 will not receive this benefit.

NOTE 8 – DESIGNATED ASSETS

The Ottumwa Water Works has designated assets comprised of demand deposits, passbook savings, and certificates of deposits that are to be used for a specific purpose. A summary of the designated assets is as follows:

Meter Deposit Fund – This fund is used to account for cash collected on customer deposits. The amount designated for the meter deposit fund as of December 31, 2008 is \$180,000.

NOTE 9 – RELATED PARTY TRANSACTIONS

The Water Works provides billing and collection services to the City of Ottumwa for sewer and refuse services. The following is a summary of the balances due to the City at December 31, 2008:

Accrued sewer services charges	\$ 603,714
Accrued refuse collection fees	<u>205,747</u>
Total accrued sewer and refuse collections	\$ <u>809,461</u>

NOTE 10 – LONG-TERM DEBT

A summary of the changes in long-term liabilities for the year ended December 31, 2008, is as follows:

	Balance Beginning Of Year	Increases	Decreases	Balance End Of Year	Due Within One Year
Revenue Bonds	\$ 7,967,129	\$ 506,870	\$ 336,999	\$ 8,137,000	\$ 355,000
Contract Payable	-	<u>570,180</u>	<u>20,686</u>	<u>549,494</u>	<u>21,358</u>
Total	\$ <u>7,967,129</u>	\$ <u>1,077,050</u>	\$ <u>357,685</u>	\$ <u>8,686,494</u>	\$ <u>376,358</u>

Annual debt service requirements to maturity for revenue bonds are as follows:

Maturing Year Ending December 31, Fully Matured	Interest Rate Various	Outstanding Amount \$ <u>7,000</u>	Interest \$ <u>1,562</u>
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OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS

NOTE 10 – LONG-TERM DEBT (Continued)

The resolutions providing for the issuance of the above revenue bonds include the following provisions:

- (a) The bonds will only be redeemed from the future earnings of the enterprise activity and the bond holders hold a lien on the future earnings of the funds.
- (b) Sufficient monthly cash transfers shall be made to a water revenue bond sinking account for the purpose of making bond principal and interest payments when due.
- (c) Additional monthly cash transfers shall be made to a bond and interest reserve account until there has been accumulated an amount equal to two years' interest on the bonds then outstanding. This account is restricted for the purpose of paying bond principal and interest should funds be insufficient in the water revenue bond sinking account.
- (d) In addition, there shall be deposited to a capital improvement and extension account the sum of \$3,000 each month until there has been accumulated a sum of \$500,000. This account shall be used solely and only to pay bonds and interest should deficiencies exist in the water revenue bond sinking account or the bond and interest reserve account to pay subordinate revenue bonds issued to make necessary improvements and extensions to pay for capital improvements and extensions to the existing Water Works' plan not covered by issuance of bonds and to call and redeem such bonds as they may be then subject to redemption prior to maturity.
- (e) There shall also be paid into a bond redemption account on a monthly basis one-half of the balance of net earnings remaining after first making the required payments into the water revenue bond sinking account, the bond and interest reserve account and the capital improvement and extension account. This account is restricted to remedying any deficiency in the other required accounts. The Water Works reserves, in the aforementioned accounts, exceed the outstanding bond and interest amounts and therefore, this provision does not apply.

Contract Payable to City of Ottumwa, Iowa

On August 15, 2006, the Water Works entered into an agreement with the City of Ottumwa, Iowa, which was related to the City's sewer separation project. In the agreement, the Water Works agreed to reimburse the City for the cost of the project that related to water main replacement. The City of Ottumwa, Iowa has paid for the entire cost of the project by issuing revenue bonds and the Water Works will pay the City of Ottumwa, Iowa for its portion of the project. The Water Works will repay the City of Ottumwa, Iowa in twenty annual installments, including interest at 3.25%. Repayment began on June 1, 2008.

Iowa Department of Natural Resources

On June 2, 2005, the Utility entered into agreements with the Iowa Department of Natural Resources and Wells Fargo Bank Iowa, N.A. for the issuance of \$4,000,000 of water revenue bonds, with an interest rate of 3.0% per annum. The bonds were issued pursuant to the provisions of Chapter 384 and Section 384.24A of the Code of Iowa to pay the costs of constructing improvements and extensions to the water system.

On December 28, 2006, the Utility entered into agreements with the Iowa Department of Natural Resources and Wells Fargo Bank Iowa, N.A. for the issuance of \$4,800,000 of water revenue bonds, with an interest rate of 3.0% per annum. The bonds were issued pursuant to the provisions of Chapter 384 and Section 384.24A of the Code of Iowa to pay the costs of constructing improvements and extensions to the water system.

OTTUMWA WATER WORKS

NOTES TO FINANCIAL STATEMENTS

NOTE 10 – LONG-TERM DEBT (Continued)

At December 31, 2008, the Utility had drawn \$8,795,000, including initiation fees of \$109,628. Wells Fargo Bank Iowa, N.A. has the remaining balances of each issue held in trust, which the Utility will request as the projects progress.

Expected repayment schedules for all of the Utility's long-term debt are as follows:

<u>Year Ended</u> <u>December 31,</u>	<u>Fully</u> <u>Matured</u>	<u>City of</u> <u>Ottumwa</u>	<u>IDNR</u> <u>SRF</u>	<u>Total</u>
2009	\$ 7,000	\$ 21,358	\$ 348,000	\$ 376,358
2010	-	22,052	358,000	380,052
2011	-	22,769	368,000	390,769
2012	-	23,508	380,000	403,508
2013	-	24,273	391,000	415,273
2014 to 2018	-	133,721	2,138,000	2,271,721
2019 to 2023	-	156,910	2,480,000	2,636,910
2024 to 2026	-	<u>144,903</u>	<u>1,667,000</u>	<u>1,811,903</u>
	\$ <u>7,000</u>	\$ <u>549,494</u>	\$ <u>8,130,000</u>	\$ <u>8,686,494</u>

NOTE 11 – RISK MANAGEMENT

The Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. The Utility assumes liability for any deductibles and claims in excess of coverage limitations.

NOTE 12 – MAJOR CUSTOMERS

Sales to three major customers accounted for greater than 50% of total sales for the year ended December 31, 2008. At December 31, 2008, amounts due from these customers were \$202,413.

NOTE 13 – COMMITMENTS AND CONTINGENCIES

The Utility has signed various contracts for current construction projects in conjunction with the City of Ottumwa, Iowa. Amounts on those contracts will be paid as progress on the projects occurs.

Prior to December 31, 2008, the Utility was named in a lawsuit by an employee. The case is in the early stages and the ultimate outcome of the case is presently uncertain. The accompanying financial statements do not include any adjustments that might be necessary should the case result in an unfavorable outcome.

NOTE 14 – RECLASSIFICATIONS

Certain amounts for 2007 have been reclassified to conform with 2008 presentation.

NOTE 15 – PRIOR PERIOD ADJUSTMENT

During 2008, certain errors resulting in a \$35,862 understatement of previously reported expenses were discovered. As a result, expenses for the year ended December 31, 2007 have been increased by \$35,862. This resulted in the following changes to net assets as of December 31, 2007:

As previously reported December 31, 2007	\$ 22,244,070
Adjustments	<u>(35,862)</u>
As restated December 31, 2007	\$ <u>22,208,208</u>

REQUIRED SUPPLEMENTARY INFORMATION

OTTUMWA WATER WORKS

BUDGETARY COMPARISON SCHEDULE OF
RECEIPTS, DISBURSEMENTS AND CHANGES IN
BALANCES - BUDGET AND ACTUAL
YEAR ENDED DECEMBER 31, 2008

	<u>Actual</u>	<u>Adjustments</u>	<u>Net</u>	<u>Budget</u>	<u>Variance Favorable (Unfavorable)</u>
Receipts:					
Use of money and property	\$ 223,954	\$ -	\$ 223,954	\$ 150,000	\$ 73,954
Charges for service	<u>4,656,224</u>	<u>-</u>	<u>4,656,224</u>	<u>4,456,089</u>	<u>200,135</u>
	<u>4,880,178</u>	<u>-</u>	<u>4,880,178</u>	<u>4,606,089</u>	<u>274,089</u>
Disbursements:					
Business-type activities	4,547,213	(1,026,412)	3,520,801	3,909,587	388,786
Capital projects/debt service	<u>-</u>	<u>1,957,219</u>	<u>1,957,219</u>	<u>1,466,250</u>	<u>(490,969)</u>
	<u>4,547,213</u>	<u>930,807</u>	<u>5,478,020</u>	<u>5,375,837</u>	<u>(102,183)</u>
Excess (deficiency) of receipts over (under) disbursements	332,965	(930,807)	(597,842)	(769,748)	171,906
Other financing sources, net	<u>-</u>	<u>1,077,050</u>	<u>1,077,050</u>	<u>700,000</u>	<u>377,050</u>
Excess (deficiency) of receipts and other financing sources over (under) disbursements	\$ <u>332,965</u>	\$ <u>146,243</u>	\$ <u>479,208</u>	\$ <u>(69,748)</u>	\$ <u>548,956</u>

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION - BUDGETARY REPORTING

YEAR ENDED DECEMBER 31, 2008

The budgetary comparison is presented as Required Supplementary information in accordance with Government Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences.

In accordance with the Code of Iowa, the Utility annually adopts a budget on the modified accrual basis following required public notice and hearing for all funds. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures.

Formal and legal budgetary control is based upon nine major classes of expenses known as functions, not by fund. These nine functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects and business-type activities. Although the budget document presents function expenses by fund, the legal level of control is at the aggregated function level, not by fund. During the year, there were no budget amendments.

During the year ended December 31, 2008, disbursements exceeded the amounts budgeted.

OTHER SUPPLEMENTARY INFORMATION

OTTUMWA WATER WORKS

DETAIL SCHEDULE OF REVENUES AND EXPENSES
YEAR ENDED DECEMBER 31, 2008

OPERATING REVENUE :

Sale of water	\$ 3,518,691
Sale of electricity	831,327
Miscellaneous income:	
Fire protection - Private	110,487
Customer forfeitures	26,012
Service connections	37,102
Service charge - Sewer billing	49,466
Service charge - Refuse billing	23,800
Miscellaneous	59,339
	<u>4,656,224</u>
TOTAL OPERATING REVENUE	

OPERATING EXPENSES:

Production:

Supervision	58,844
Maintenance labor	75,949
Operations labor	198,316
Chemicals/carbon	325,375
Laboratory supplies	14,965
	<u>673,449</u>

Distribution:

Supervision	23,854
Maintenance labor	251,983
Maintenance materials	164,773
Labor	129,898
Contract street repairs	117,412
	<u>687,920</u>

Hydro:

Supervision	6,637
Operations labor	81,552
Supplies	29,012
Lease and rentals	14,158
Contract Labor	1,611
	<u>132,970</u>

Financial services:

Financial services supervision	53,494
Financial services labor	106,515
Office supplies	17,198
Postage expense	50,094
Interest expense	28,951
Customer deposit accounts interest	3,033
Noncollectible accounts	16,500
	<u>275,785</u>

OTTUMWA WATER WORKS

DETAIL SCHEDULE OF REVENUES AND EXPENSES
YEAR ENDED DECEMBER 31, 2008

OPERATING EXPENSES: (Continued)

Administration:

Executive salaries	73,842
Board salaries	2,090
Training expense	6,070
Vacation pay	61,001
Holiday expense	49,490
Longevity expense	15,281
Casual pay	17,077
Sick pay	9,241
Disability	21,048
Payroll tax - FICA	92,803
Payroll tax - IPERS	73,387
Subscriptions	234
Legal services	25,188
Business expense	20,758
	<u>467,510</u>

General plant:

Employee's miscellaneous expense	18,541
General property expense	110,880
Safety program	17,509
Liability insurance	69,897
Workmen's compensation insurance	24,702
Group health insurance	353,747
Group term life insurance	3,050
Health insurance - Retirees	31,460
Flood	63,678
Contract labor	82,014
Fuel and power	346,343
General services	84,845
Contingency	34,122
Gas and oil	42,179
Lease and rental	200
	<u>1,283,167</u>

Depreciation and amortization 1,026,412

TOTAL OPERATING EXPENSES 4,547,213

OPERATING INCOME 109,011

NONOPERATING REVENUE:

Interest income 223,954

CHANGE IN NET ASSETS \$ 332,965

INDEPENDENT AUDITOR'S REPORT ON INTERNAL
CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Board of Trustees
Ottumwa Water Works
Ottumwa, Iowa

We have audited the accompanying financial statements of Ottumwa Water Works, as of and for the year ended December 31, 2008, and have issued our report thereon dated August 7, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Ottumwa Water Works' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Ottumwa Water Works' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Ottumwa Water Works' internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects Ottumwa Water Works' ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood a misstatement of Ottumwa Water Works' financial statements that is more than inconsequential will not be prevented or detected by Ottumwa Water Works' internal control. We consider the deficiencies described in the accompanying Schedule of Findings to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood a material misstatement of the financial statements will not be prevented or detected by Ottumwa Water Works' internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we believe items I-A-08 and I-B-08 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters required to be reported under Government Auditing Standards.

Comments involving statutory and other legal matters about the Utility's operations for the year ended December 31, 2008 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Utility. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

Ottumwa Water Works' responses to findings identified in our audit are described in the accompanying Schedule of Findings. While we have expressed our conclusions on the Utility's responses, we did not audit Ottumwa Water Works' responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials and customers of the Utility and other parties to whom the Utility may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Ottumwa Water Works during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

ANDERSON, LARKIN & CO P.C.

Ottumwa, Iowa
August 7, 2009

OTTUMWA WATER WORKS
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2008

Part I: Findings Related to the Financial Statements

SIGNIFICANT DEFICIENCIES:

- I-A-08 Segregation of Duties - An important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible.

Recommendation - We realize that with a limited number of office employees, segregation of duties is difficult. However, the Utility should review its control procedures to obtain the maximum internal control possible under the circumstances

Response - We will continue to institute segregation and rotation of employee's duties wherever possible in relation to our staff size

Conclusion - Response accepted.

- I-B-08 Prior Period Adjustment - During the audit for the year ended December 31, 2008, it was determined that depreciation expense of \$35,862 was erroneously omitted from the financial statements for the year ended December 31, 2007.

Recommendation - The Utility should implement policies and procedures to avoid possible future omissions

Response - We will do so

Conclusion - Response accepted

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

Part II: Other Findings Related to Required Statutory Reporting

- II-A-08 Certified Budget - Disbursements during the year ended December 31, 2008 exceeded the amounts budgeted. The Code of Iowa states, in part, "Public monies may not be expended or encumbered except under an annual or continuing appropriation"

Recommendation - The budget should have been amended in accordance with the Code of Iowa before disbursements were allowed to exceed the budget.

Response - The budget will be amended in the future, if applicable.

Conclusion - Response accepted.

- II-B-08 Questionable Expenses - No expenses we believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979 were noted.

- II-C-08 Travel Expense - No expenditures of money for travel expenses of spouses of Utility officials or employees were noted.

- II-D-08 Business Transactions - No business transactions between the Utility and Utility officials or employees were noted.

OTTUMWA WATER WORKS
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2008

Part II: Other Findings Related to Required Statutory Reporting (Continued)

- II-E-08 Bond Coverage - Surety bond coverage of Utility officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations
- II-F-08 Trustee Minutes - No transactions were found that we believe should have been approved in the minutes but were not
- II-G-08 Revenue Bonds - The Water Works has complied with the revenue bond provisions.
- II-H-08 Deposits and Investments - No instances of noncompliance with the deposit and investment provisions of Chapter 12B and 12C of the Code of Iowa were noted.